(3)

No. 90-1853

Supreme Court, U.S.
FILED
JUL 16 1991
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

NATIONWIDE CORPORATION AND
NATIONWIDE MUTUAL INSURANCE COMPANY,
Petitioners,

v.

HOWING COMPANY AND DOUGLAS MCLELLAN,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

---

REPLY BRIEF FOR THE PETITIONERS

JEFFREY S. DAVIDSON
(Counsel of Record)
KIRKLAND & ELLIS
300 South Grand Avenue
Suite 3000
Los Angeles, California 90071
(213) 680-8400

DANIEL F. ATTRIDGE
YOSEF J. RIEMER
KAREN N. WALKER
DOUGLAS W. HALL
KIRKLAND & ELLIS
655 Fifteenth Street, N.W.
Washington, D.C. 20005
(202) 879-5000

Counsel for Petitioners Nationwide Corporation and Nationwide Mutual Insurance Company

Dated: July 16, 1991

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

I. *VIRGINIA BANKSHARES* MAKES CLEAR THAT THE SIXTH CIRCUIT'S APPLICATION OF A PRESUMPTION OF MATERIALITY CONFLICTS WITH THIS COURT'S DECISION IN *TSC INDUSTRIES* 2

II. THE SIXTH CIRCUIT'S IMPLICATION OF A PRIVATE RIGHT OF ACTON UNDER SECTION 13(e) CONFLICTS WITH *VIRGINIA BANKSHARES* AND OTHER DECISIONS OF THIS COURT 5

CONCLUSION 9

TABLE OF AUTHORITIES

Cases: Page

Alton Box Board Co. v. Goldman, Sachs & Co., 560 F.2d 916 (8th Cir. 1977) 3
Basic Inc. v. Levinson, 485 U.S. 224 (1988) 3, 4
Berg v. First American Bankshares, Inc., 796 F.2d 489 (D.C. Cir. 1986) 3
Cannon v. University of Chicago, 441 U.S. 677 (1979) 6, 7
Cort v. Ash, 422 U.S. 66 (1975) 7
Levine v. NL Industries, Inc., 926 F.2d 199 (2d Cir. 1991) 4
Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 456 U.S. 353 (1982) 7
Reeves v. Continental Equities Corp. of America, 912 F.2d 37 (2d Cir. 1990) 8
Siebert v. Conservative Party, 724 F.2d 334 (2d Cir. 1983), *cert. denied*, 466 U.S. 980 (1984) 8
Texas & Pacific R. Co. v. Rigsby, 241 U.S. 33 (1916) 7
Touche Ross & Co. v. Redington, 442 U.S. 560 (1979) 1-2, 5, 6
Transamerica Mortgage Advisors, Inc. v. Lewis, 444 U.S. 11 (1979) 5-6
TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976) 1, 3
United States v. Bilzerian, 926 F.2d 1285 (2d Cir. 1991) 5
Virginia Bankshares, Inc. v. Sandberg, 59 U.S.L.W. 4887 (June 27, 1991) ..... *passim*

Statutes and Rules:

Securities Exchange Act of 1934
Section 10(b), 15 U.S.C. § 78j(b) (1988) 3
Section 13(e), 15 U.S.C. § 78m(e) (1988) 3, 5, 6, 7
Section 14(a), 15 U.S.C. § 78n(a) (1988) 3, 6, 7
Section 18(a), 15 U.S.C. § 78r(a) (1988) 6

SEC Regulation S-K, 17 C.F.R. § 229.101(c)(1)(xii) (1990) 4

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

No. 90-1853

NATIONWIDE CORPORATION AND
NATIONWIDE MUTUAL INSURANCE COMPANY,
Petitioners,

v.

HOWING COMPANY AND DOUGLAS MCLELLAN,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

---

REPLY BRIEF FOR THE PETITIONERS

Since the filing of this petition, this Court's decision in *Virginia Bankshares, Inc. v. Sandberg*, 59 U.S.L.W. 4887 (June 27, 1991), has confirmed that the Sixth Circuit's decisions in this case are in conflict with the decisions of this Court. *First*, in *Virginia Bankshares*, this Court applied the materiality standard set forth in *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438 (1976), to determine materiality in the context of a going-private merger, but the Sixth Circuit held that a "heightened" standard under which materiality must be "presumed" is applicable to going-private mergers. *Compare* 59 U.S.L.W. at 4888 *with* 3a-5a. *Second, in Virginia Bankshares*, this Court reaffirmed the holding of *Touche Ross*

& Co. v. Redington, 442 U.S. 560 (1979), that Congressional silence cannot be considered positive evidence of the legislative intent that is required to imply a private damages action, but the Sixth Circuit treated Congressional silence as *support* for implying a private damages action. *Compare* 59 U.S.L.W. at 4892 *with* 42a, 44a-45a.

While *Virginia Bankshares* underscores the importance of granting certiorari, respondents never mention it. Nor do respondents offer any rationale for the Sixth Circuit's departures from this Court's prior precedents or any persuasive means of distinguishing the conflicting decisions of other circuits that the Sixth Circuit also ignored. Respondents also say nothing about the exceptional importance of this case given the enormous uncertainty it creates in an area involving a substantial portion of all takeovers and billions of dollars in transactions each year. In sum, nothing in respondents' brief in any way diminishes the compelling reasons for granting the writ set out in the petition.

I. *VIRGINIA BANKSHARES* MAKES CLEAR THAT THE SIXTH CIRCUIT'S APPLICATION OF A PRESUMPTION OF MATERIALITY CONFLICTS WITH THIS COURT'S DECISION IN *TSC INDUSTRIES*.

This Court's recent decision in *Virginia Bankshares* highlights that the Sixth Circuit's ruling that a "heightened" materiality standard should be applied in going-private mergers is inconsistent with decisions of this Court. Like the case at bar, *Virginia Bankshares* involved a going-private (or what this Court called a "freeze-out") merger in which plaintiffs challenged the sufficiency of a proxy statement's description of the directors' views as to the "fairness" of the transaction. *Compare* 59 U.S.L.W. at 4888 *with* 1a-2a. This Court held that even a "conclusory" statement falsely reporting that the directors believed the freeze-out transaction to be fair would be inactionable if immaterial. Relying on *TSC*, the Court de-

clared that liability under the securities laws "must rest not only on deceptiveness but materiality as well (*i.e.*, it has to be significant enough to be important to a reasonable investor deciding how to vote, *see TSC Industries*, 426 U.S. at 449)." 59 U.S.L.W. at 4888. Thus *Virginia Bankshares*, like this Court's earlier decision in *Basic Inc. v. Levinson*, 485 U.S. 224, 240 n.18 (1988), rejected the position that the Sixth Circuit adopted in this case: that a different standard should apply in judging materiality in going-private or "freeze-out" mergers.

Ignoring *Virginia Bankshares* and *Basic*, respondents assert that: (1) *TSC* does not control because it was decided under Section 10(b), not Section 13(e) of the Securities Exchange Act; and (2) the Sixth Circuit's "presumption of materiality" is somehow "consistent" with *TSC*. Neither contention has any merit.

First, *TSC* (which was actually decided under Section 14(a), 426 U.S. at 449) has been applied by this Court and the courts of appeals to judge materiality under *all* of the securities statutes [1] and the D.C. Circuit so interpreted *TSC* in applying it to Section 13(e) in *Berg v. First American Bankshares, Inc.*, 796 F.2d 489, 495, 502 (D.C. Cir. 1986).[2] Significantly, respondents offer no persuasive rationale—indeed, no rationale at all—for believing that a different "heightened" standard should apply to cases brought under Section 13(e) or that any "presumption of materiality" is appropriate in this context. And to the extent the Sixth Circuit assumed a different

---

[1] *See, e.g., Basic*, 485 U.S. at 240 (*TSC* not limited to Section 14(a) context but applied to Section 10(b)); *Alton Box Board Co. v. Goldman, Sachs & Co.*, 560 F.2d 916, 919-20 (8th Cir. 1977) ("the test of materiality is the same under all the securities statutes").

[2] Respondents' argument that *Berg* "did not address a violation of Section 13(e) or Rule 13e-3" (Resp. Br. at 6) is flat wrong. The basis for the *Berg* court's finding of no RICO violation was its conclusion that omissions deemed immaterial under *TSC* could not give rise to culpability under Section 13(e). 796 F.2d at 495, 502.

standard was required if a proxy statement involved a going-private merger or the alleged omission of information required by an SEC schedule or regulation, the Sixth Circuit's decision conflicts with this Court's decisions in *Basic* and *Virginia Bankshares* as well as such other appellate decisions as *Levine v. NL Industries, Inc.*, 926 F.2d 199 (2d Cir. 1991).[3]

Second, despite respondents' effort to reconcile the Sixth Circuit's "heightened" materiality standard with *TSC*, the "presumption of materiality" respondents now seek to trivialize is both broad and pernicious, not narrow. To begin with, even under respondents' formulation, materiality is automatically presumed "when[ever] the SEC mandates the disclosure of certain facts." (Resp. Br. at 5.) But the SEC has promulgated 179 forms and schedules requiring thousands of items of information under the 1933 and 1934 Acts. Under this supposedly narrow presumption, for example, a court would presume the materiality of an omission of the address of the issuer of a proxy statement (required by Item 1 of Schedule 13E-3).

Tellingly, respondents offer no indication of how any issuer of a proxy statement can ever overcome a "presumption of materiality." This is because, when applied to specific factual circumstances, the Sixth Circuit's "presumption of materiality" becomes outcome determinative. But for that presumption, respondents would have lost as a matter of law under *TSC*. The Sixth Circuit's application of the presumption in this case led it to deem material the information about after-the-fact valuations and

---

[3] *See, e.g., Virginia Bankshares*, 59 U.S.L.W. at 4888; *Basic*, 485 U.S. at 240 n.18; *Levine*, 926 F.2d at 202-03. Respondents are wrong in asserting that "[t]here was no specific disclosure requirement promulgated by the SEC" at issue in *Levine*. (Resp. Br. at 7.) To the contrary, *Levine* applied *TSC* to judge the materiality of an omission of a disclosure required by SEC Regulation S-K, 17 C.F.R. § 229.101(c)(1)(xii) (1990). 926 F.2d at 202-03.

"comparable" transactions that other courts of appeals, correctly applying *TSC*, have held immaterial. (*See* Petition at 19-20.) Like the *per se* materiality standard respondents urged below and the Second Circuit rejected in *United States v. Bilzerian*, 926 F.2d 1285, 1298 (2d Cir. 1991), the Sixth Circuit's "heightened" standard does what no other federal court has been willing to do: it allows a finding of materiality in contravention of *TSC*.

In sum, *Virginia Bankshares* underscores, and nothing in respondents' opposition detracts from, the need for certiorari to review the Sixth Circuit's decision on the materiality issue in this case.[4]

II. THE SIXTH CIRCUIT'S IMPLICATION OF A PRIVATE RIGHT OF ACTION UNDER SECTION 13(e) CONFLICTS WITH *VIRGINIA BANKSHARES* AND OTHER DECISIONS OF THIS COURT.

This Court's decision in *Virginia Bankshares* also confirms that the Sixth Circuit's holding that a private right of action should be implied under Section 13(e) is inconsistent with Supreme Court precedent. Certiorari should be granted to resolve this conflict as well.

Virginia Bankshares reaffirmed the holding of *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979), and *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S.

---

[4] Materiality was the focus of the remand proceedings before the district court because of the Sixth Circuit's prior instructions that the threshold area of inquiry should be the issue of materiality. (57a.) Nationwide reserved the right to assert additional defenses, including lack of causation. It is clear that plaintiffs' claims are deficient in light of this Court's *Virginia Bankshares* decision because Nationwide, like the defendant in *Virginia Bankshares*, did not require the minority shareholders' votes to authorize the going-private merger. (69a.) In *Virginia Bankshares*, the Court held that there was no causation of damages compensable under the Securities Exchange Act for shareholders whose votes were not required by law or corporate bylaw to authorize a corporate action subject to a proxy solicitation. 59 U.S.L.W. at 4891-93.

11 (1979), that legislative silence *cannot* be considered positive evidence of the Congressional intent required to imply a private damages action. To the contrary, *Virginia Bankshares* held that Congressional silence regarding an intent to recognize a more expansive cause of action under Section 14(a) was a "serious obstacle" which the plaintiff in that case would have to (and could not) overcome.[5] The Sixth Circuit, on the other hand, considered Congressional silence as *support* for its holding that Congress intended that courts imply private damages actions under Section 13(e). (*See* 42a, 44a-45a.)

Virginia Bankshares also rejected the Sixth Circuit's view that the "contemporary legal context" under which a statute was enacted includes the then-existing Supreme Court test for implying private rights of actions.[6] The

---

[5] *See Virginia Bankshares*, 59 U.S.L.W. at 4892; *see also Touche Ross*, 442 U.S. at 571 ("implying a private right of action on the basis of Congressional silence is a hazardous enterprise, at best"); *Transamerica*, 444 U.S. at 18 (Congressional silence "is not inevitably inconsistent with" and "does not automatically undermine" a finding of Congressional intent).

In addition, *Virginia Bankshares* reaffirmed the principle expressed in *Touche Ross*, *Transamerica*, and other cases that private rights of action should not be implied where Congress has expressly provided other remedies in the same statute. *See Virginia Bankshares*, 59 U.S.L.W. at 4892-93 ("we would have trouble inferring any congressional urgency to depend on implied private actions to deter violations of § 14(a), when Congress expressly provided private rights of action in §§ 9(e), 16(b) and 18(a) of the same Act"). Similarly, the existence of an express private right of action under Section 18(a) in this case counsels against implying a private right of action under Section 13(e). *See* Petition at 22-23.

[6] The "contemporary legal context" theory was first announced by this Court in *Cannon v. University of Chicago*, 441 U.S. 677 (1979), and represented a narrow exception to the general rule that courts will not imply private rights of action in the face of Congressional silence: if a statute was explicitly patterned after an existing law, and if courts had overwhelmingly held before enactment of the second statute that there was a private right of action under the existing statute, then a court was permitted to assume that the

statute at issue in *Virginia Bankshares* was enacted in 1934, when this Court's test for determining whether to imply a private right of action was *Texas & Pacific R. Co. v. Rigsby*, 241 U.S. 33 (1916).[7] Under *Rigsby*, "the denial of a remedy [was] the exception rather than the rule," *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 375 (1982), and courts implied private rights of action in the face of Congressional silence on the issue. Thus, under the Sixth Circuit's theory, the *Virginia Bankshares* Court should have used the *Rigsby* test to determine the scope of an implied right of action under Section 14(a), and because of Congress' silence on the issue, the Court would have been forced to conclude that Congress intended the remedy to exist.[8] This, of course, the Court did not do; instead it applied the analysis set forth in *Touche Ross*—the current test for determining whether to imply private right of actions—decided in 1979. 59 U.S.L.W. at 4892. It is clear, therefore, that the Sixth Circuit's theory dangerously miscomprehends and misapplies the contemporary legal context doctrine as enunciated by this Court.

Respondents fail even to mention *Virginia Bankshares*, much less attempt to distinguish it or any of the cases discussed in the petition regarding the proper standard for implying private rights of action. Respondents say only

---

legislature was "familiar with these unusually important precedents from this and other federal courts and that it expected its enactment to be interpreted in conformity with them." *Id.* at 699.

[7] *Rigsby* was also the test in effect in 1968 when Section 13(e) was enacted. The Sixth Circuit described this period as one in which "implied rights of action were in a heyday of sorts." (44a.) *Rigsby* was supplanted by *Cort v. Ash*, 422 U.S. 66 (1975), which in turn has been further refined by *Touche Ross*. *See Virginia Bankshares*, 59 U.S.L.W. at 4892; Petition at 25 n.28.

[8] *See* 44a ("Since there is no evidence of legislative intent to deny a private remedy, Congress' choice to incorporate the proxy rules without additional comment is an indication of legislative intent sufficient to satisfy the second *Cort* test.").

that the Sixth Circuit's decision to rely on Congressional silence as support for implying a private right of action, despite *Touche Ross*, *Transamerica*, and *Cannon*, "does not create a conflict between Circuit Courts." (Resp. Br. at 7.) Respondents are wrong on this point.[9] But even more important, respondents overlook the fact that the Sixth Circuit's decision represents a radical departure from *Supreme Court* precedent which in and of itself justifies the granting of the petition. Respondents also have failed to address the great significance of this case: not only to the large number of transactions covered by the Sixth Circuit's holding, but also the far-reaching implications for other statutes if Congressional silence can be read as supporting an implied damages action.

---

[9] The Sixth Circuit is in conflict with the Second Circuit, which has held that the Sixth Circuit's approach would distort *Cannon* into a rule "that the law must be frozen in time for purposes of determining whether Congress intended an implied right of action to exist." *Siebert v. Conservative Party*, 724 F.2d 334, 337 (2d Cir. 1983), *cert. denied*, 466 U.S. 980 (1984); *see also Reeves v. Continental Equities Corp. of America*, 912 F.2d 37, 40-41 (2d Cir. 1990).

CONCLUSION

For the foregoing reasons, and for those stated in the petition, a writ of certiorari should be granted.

Respectfully submitted,

JEFFREY S. DAVIDSON
(Counsel of Record)
KIRKLAND & ELLIS
300 South Grand Avenue
Suite 3000
Los Angeles, California 90071
(213) 680-8400

DANIEL F. ATTRIDGE
YOSEF J. RIEMER
KAREN N. WALKER
DOUGLAS W. HALL
KIRKLAND & ELLIS
655 Fifteenth Street, N.W.
Washington, D.C. 20005
(202) 879-5000

Counsel for Petitioners Nationwide Corporation and Nationwide Mutual Insurance Company

Dated: July 16, 1991